RESEARCH HIGHLIGHT

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Survey of Issues and Challenges to Providing Market Housing Finance in the Territories

INTRODUCTION

According to 2006 Census data, both homeownership rates and private market rental housing rates in the Canadian territories are generally much lower than those in the rest of Canada. In fact, in many smaller communities there is very little, if any, market housing. The lack of adequate finance has been suggested as a possible cause of these issues. This exploratory study endeavoured to identify any issues and challenges that may be affecting market housing finance in the Canadian territories.

RESEARCH OBJECTIVES

The overall objectives for the study were as follows:

- To provide an understanding of issues affecting mortgage lending and construction financing in existing and emerging markets in the territories.
- To identify the circumstances, challenges and gaps affecting market housing finance.
- To discuss the significance of the identified circumstances, challenges, and gaps to the growth of market housing in the territories.

METHODOLOGY

There were two distinct phases to this exploratory study: 1) a review of available literature; and 2) interviews with key informants and focus groups that were conducted in eight communities. The following eight communities were selected based on their size and potential for expanding housing markets: Hay River (N.W.T.), Inuvik (N.W.T.), Yellowknife, (N.W.T.), Iqaluit (Nun.), Cambridge Bay (Nun.), Rankin Inlet (Nun.), Dawson City (Y.T.), and Whitehorse (Y.T.).

Review of available literature

An initial literature review was conducted to determine what is currently known about the circumstances, challenges and gaps impacting market housing finance in the territories. Documents reviewed were obtained from various sources, including, but not limited to, federal and territorial governments, professional organizations, academics, non-profit organizations and media. They included research reports and statistics, scholarly articles, news articles, websites, and presentations.

Canada

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HOME TO CANADIANS

Interviews with key informants and focus groups

Face-to-face and/or phone interviews were conducted with landlords and real estate development companies, government representatives, lenders, real estate agents, individual and potential homebuyers in the territories, and others[1] associated with the housing market and/or housing financing in the territories. Focus groups were held with lenders, developers, municipal staff, territorial housing corporation staff, and Aboriginal officials.

LIMITATIONS

The research was limited by the small sample size of eight communities. While care was taken that the selected communities were diverse in location and size, the results may not accurately reflect the situation in all communities in the territories.

The research was aiso limited by the number of homebuyers available to be interviewed in comparisc.n to the other groups of key informants.

It is important to note that the study is exploratory and relies on secondary research such as a review of available literature and response from key informants. Rather than attempt to draw definitive conclusions, the study seeks to help identify and define the issues.

RESEARCH FINDINGS

This research identifies some of the key issues and challenges affecting mortgage lending and construction financing in the context of the particular landscape of the Canadian territories, and identifies borrower and service provider insights relating to them.

1. The landscape of the territories

Geography, population and climate

At 40% of Canada's land mass, the territories account for a huge geographic area. However, the territories are one of the most sparsely populated areas of the world. The total population of the three territories in 2011 was just over 100,000. Of this relatively small overall population, 46% of the population lives in the three territorial capitals, with

Teslin, Yukon
Credit: CMHC

77% of the Yukon population living in Whitehorse, 46% of the Northwest Territory (N.W.T.) population living in Yellowknife, and 20% of the Nunavut population living in Iqaluit. Eleven per cent of the territories' population lives in the non-capital communities where key informants were interviewed for this study, and the remaining 43% are spread out over 83 other communities, many of which are remote and inaccessible by road. These non-capital communities are mostly small, remote, and have limited transportation infrastructure. The region also faces extreme weather conditions (winters can get as cold as -40 degrees Celsius and the harsh weather conditions can last as long as eight months a year in some communities).

The territories are not a homogeneous region—it is a diverse area with a culturally diverse population living in widely differing circumstances. A large portion of the population in the territories is Aboriginal. The proportion of Aboriginal to non-Aboriginal populations varies across the North. According to 2006 data, Yukon has the lowest proportion at 25% of its total population; in the Northwest Territories, one-half of the population is Aboriginal; and in Nunavut, more than 85% of the territory's population is Inuit.

Land tenure

There are many different forms of land tenure in the territories. In the Northwest Territories, for example, there are six forms of land tenure. In addition to private ownership and land claims areas, there are Commissioner's

[1] "Other" includes a housing consultant, realtors, appraisers, a chamber of commerce member and a Habitat for Humanity representative.

lands, federal lands, Indian Affairs Branch lands and Indian reserves. In Nunavut, there are at least three forms of tenure in addition to private ownership, and in Yukon, there are four. Some types of land in the territories cannot be mortgaged.

Economy

Communities in the territories are, in general, less economically diverse than in the South, with the resident population relying heavily on natural resource extraction and the public sector for employment. While the public sector provides relative stability, with secure and well-paying jobs, the resource sector can be volatile due to wide swings in global resource demand. However, despite the volatility of the resource sector and the negative impact of the 2008/2009 global economic crisis, the current economic forecast for the territories is generally positive.[2] Although the N.W.T. economy slowed in 2011, Yukon and Nunavut experienced significant growth. Strong resource sector exploration and development is expected to continue to contribute to economic growth in all three territories. Even Nunavut's economy is rebounding after a five-year absence of metal mining activity. The Meadowbank gold mine commenced in 2010 and several other mining projects are in various stages of development.[3]

Employment

In spite of the fact that the resource sector is expected to continue to contribute to economic growth and job gains in the territories, unemployment is still an issue. In some areas this may be due to increased labour force participation offsetting jobs added.[4] Unemployment can be high in many small communities because most communities outside the major centres do not have an economic base. Apart from mining towns and service centres like Whitehorse, Yellowknife and Iqaluit, many small, remote communities have few permanent, wage-based employment opportunities, which results in many low-income households and many people who rely on social assistance and/or the informal

Construction worker from Fort Liard, N.W.T.
Credit: CMHC

or "land-based" economy. There is a marked difference between the unemployment rates of the non-Aboriginal population and Aboriginal population. As of 2006, the unemployment rate for the non-Aboriginal population in Yukon was 6.2%, 4.0% in the Northwest Territories and 3.5% in Nunavut, as compared to the rest of Canada (6.6%). The unemployment rate for the Aboriginal population was significantly higher at 21.9% in Yukon, and 20.1% in both the Northwest Territories and Nunavut.[5]

Income

For those who are employed, incomes in the territories are much higher than in the rest of Canada. There is a significant difference in average income between households in the capitals and households in the smaller communities, and also between non-Aboriginal households and Aboriginal households. According to 2006 Census data, average incomes in 2005 of non-Aboriginal households in the territories were higher than the average for all households in Canada ($69,548): $76,838 in Yukon, $112,386 in the Northwest Territories and $113,109 in Nunavut. In contrast, household incomes were much lower among the Aboriginal population: $57,481 in Yukon, $70,724 in the Northwest Territories and $63,695 in Nunavut.[6]

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[2] Conference Board of Canada, *Territorial Outlook*, February 2011.

[3] Canada Mortgage and Housing Corporation, *Northern Housing Report*, 2011; *Northern Housing Report*, 2012.

[4] Canada Mortgage and Housing Corporation, *Northern Housing Report*, 2011; *Northern Housing Report*, 2012.

[5] Statistics Canada, Census 2006.

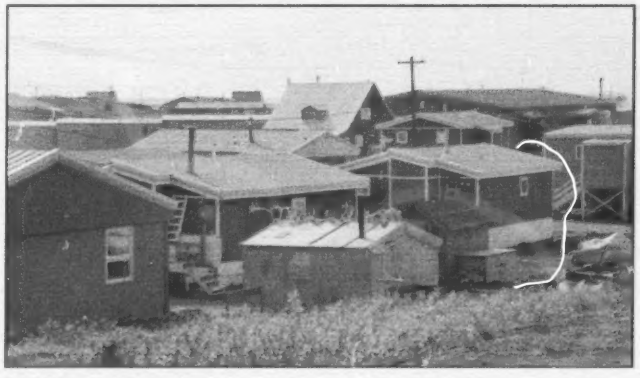
[6] Statistics Canada, Census 2006. Income reported in the Census is for the previous year; i.e., 2005 for the 2006 Census.

Cost of living

The cost of housing, food, utilities, transportation, etc. in the territories is significantly higher than in southern Canada. Houses in the territories, for example, are often more expensive than in the rest of Canada.[7] Operation and maintenance costs were also significantly higher. For example, average annual utility costs in most communities are more than double the Canadian average. For those that do find rental housing, they can expect to pay high rent. The average rent in 2011 for a two-bedroom unit in Yellowknife was $1,566 and in Iqaluit, $2,356. In Whitehorse, the average rent of $813 for a two-bedroom unit was closer to rent levels in southern Canada.[8]

Housing market

Housing tenure in the territories differs significantly from the rest of Canada. Outside of the capital cities and a few other markets, a significant proportion of households live in subsidized rental housing, such as social housing or employer-provided housing. For example, there is limited owner-occupied housing in Nunavut (20%), with most of the housing being subsidized rental housing (51%).[9] Public housing in Yukon is far less prevalent and according to the 2006 Census, 63.8% of all Yukon households lived in owner-occupied housing, almost on par with the rest of Canada. In the Northwest Territories, nearly 48% of the housing available is rental property, with 25% of all available housing being private market rental and 22% being subsidized rental.[10] These are territorial averages and the numbers can vary significantly across the communities.



Tuktoyaktuk, N.W.T.
Credit: CMHC

Housing markets vary widely across the territories. While the capitals show recent growth in areas of housing starts and resales,[11] other communities have virtually no housing market. Even with the housing market growth in the capital cities, the markets still remain relatively small. For example, in Yellowknife, with a population of approximately 20,000, CMHC expects 175 units in total housing starts and 390 residential resale transactions in 2012.[12]

Issues impeding market housing in the territories

The issues impeding market housing in the territories are related to several aspects of the landscape: the small, sparse population spread out over many very small, often remote and isolated communities; communities inaccessible by road coupled with the high costs of alternative transportation; extreme weather conditions that present challenges to construction and maintenance of housing; low incomes

[7] In Whitehorse, the average price for a home in 2011 was $362,058, while in Iqaluit it was $335,456. The average resale residential price in Yellowknife was $375,050.

[8] Canada Mortgage and Housing Corporation, *Northern Housing Report*, 2011, and *Canadian Housing Observer*, 2011

[9] Income Statistics Division, Statistics Canada for Nunavut Housing Corporation, *An Analysis of the Housing Needs in Nunavut: Nunavut Housing Needs Survey 2009/2010*, October 29, 2010.

[10] Northwest Territories Bureau of Statistics, *2009 NWT Community Survey Housing Component*, January 2010.

[11] Canada Mortgage and Housing Corporation, *Northern Housing Report*, 2011; *Northern Housing Report*, 2012.

[12] Northwest Territories Bureau of Statistics, 2010.

and high unemployment in many communities that make homeownership and even unsubsidized rent unaffordable; high costs of housing, including high maintenance and operation costs; and lack of skilled local labour. All of these factors create challenges to the expansion of market housing in the territories.

The challenging climate of the territories and remote location of many communities create logistical complexities in the availability and delivery of building materials and also labour. Materials and labour are generally not local. Materials must be transported over great distances, often by sea lift or barge delivery. Delivery of materials can often be delayed. These factors result in a substantially higher landed cost of goods. In some communities, building materials must be ordered three to six months in advance of delivery and paid for up front, often through some form of self-financing, which can be a significant impediment for individuals and smaller builders and investors.

The cost of living, as well as the operation and maintenance costs of housing in the territories, is high in comparison to incomes. Although demand for housing may be there, the incomes of those seeking housing may not be high enough to fully cover these costs. In some markets, maintenance and operating costs are significant detractors to homeownership, particularly in more isolated communities. In Nunavut, for example, the cost for heating a single-detached unit in colder months is estimated at $1,000 per month.

There is employment uncertainty for many residents of the territories. Many communities rely largely on a single-sector (resource extraction) economy and residents of smaller, remote communities often engage in informal, seasonal employment. The income uncertainty that this creates can pose practical challenges to achieving homeownership and maintaining a strong new and resale housing market.

Sea lift, Iqaluit, Nunavut
Credit: CMHC

The topography, remoteness, and the small development scale in which land is developed increases costs of developing land. As a substantial component of housing development, the high cost of land development can affect housing supply. High land costs may deter developers/contractors from building market housing because the required selling price may not be affordable or marketable to those living in or moving to the territories. Moreover, municipal governments may not have the resources to cover the costs of municipal infrastructure and servicing required to developing a sufficient supply of serviced lots for residential use.

Unique land tenures in the territories can also create issues in securing mortgage financing. The preferred forms of land tenure for securing mortgage financing from banks or other institutions are fee simple (i.e., private land ownership) or long-term leasehold. Much of the land in the territories does not neatly fit into these categories, limiting access to mortgage financing and thereby limiting homeownership.

2. FINDINGS FROM KEY INFORMANT INTERVIEWS

Key informants provided borrower and service provider insights into housing finance issues in the territories.

Construction financing and associated risks

Factors such as harsh climate and short construction seasons, remoteness and access difficulties, and shortage of local skilled labour, for example, all contribute to the logistical challenges and high costs associated with housing construction in the territories. These challenges to construction can cause delays or incompletion of work. Key informants indicated that this can sometimes make lenders more reluctant to provide financing for construction. Even when borrowers do access construction financing, there may be further difficulties in accessing draws on the financing when the funds are needed mainly due to the protracted time to complete construction work and the fact that suppliers often require payment for materials in advance. These factors can be a greater barrier for individual borrowers building their own home and for smaller builders because they do not always have the capacity to complete construction on schedule, or the cash flow resources to cover costs in cases of delays. It is less of an issue for larger builders but they still generally can carry costs for only a few units at a time.

Property appraisal issues

In assessing a loan application, it is standard mortgage underwriting practice for consideration to be given to the borrower, the market and the property before a loan can be approved. When assessing the property, there is a need to support the lending value on a property, so either comparable sales data must be available or an appraisal of the property must take place.

Key informants have confirmed that there are often limited comparable sales data available on properties in smaller communities. In lieu of comparable sales data, appraisals are often required. Because availability of appraisal services and data on comparable properties are limited in many parts of the territories, this requirement can significantly delay the financing process. Key informants claim that these factors can delay the financing process and may make lenders reluctant to consider applications—especially those applications originating from smaller, more remote communities.

Negative risk assessments

Key informants stated that lenders may be reluctant to provide mortgage financing to potential homebuyers in the territories because of the present and future marketability of the property. In determining whether to provide financing, lenders will conduct a risk assessment of the community's housing market, and assess a range of factors, including, but not limited to, market size, employment rate, economic diversity, market cycles, and market outlook. Although the economic outlook for the territories is generally positive, there is economic uncertainty in some communities, and there are communities that rely on one or a few sectors for their economic well-being. Reliance on one sector can increase the risk of lending because in the event of economic downturn, the risk of borrowers defaulting on their mortgages is expected to increase substantially. At the same time, an economic downturn is also likely to reduce the number of prospective buyers available to purchase a resale property and reduces the chances that a lender could recover the full value of the original mortgage if the home was to be resold. As a result, financing is often not readily available, and, if lenders do provide financing, they will often use insured mortgages to lessen their risk.

Rental housing investment

According to key informants, there may be less willingness for lenders to finance multi-unit rental housing due to the economic uncertainty, particularly in communities that depend largely on one sector. Key informants believe that, under these circumstances, long-term lease agreements with governments or employers for potential rental units are more favourable to lenders and investors because the vulnerability to market fluctuations is lessened. With a long-term lease agreement in place, the investor is less susceptible to market fluctuations in rents or vacancies.

Unstable markets also increase the likelihood that a surplus of rental units may occur, particularly in smaller markets where there are fewer properties to spread the burden or risk of a surplus of units. Small, unstable markets can increase the likelihood that a borrower may default, thus increasing the risk for the lender or mortgage insurance provider.

Personal financial situation of the borrower

The personal financial situation of the borrower was identified during the research as one of the key reasons as to why lenders are reluctant to provide financing for potential homeowners in the territories. It was commented during the interviews that issues with respect to lack of credit history, the borrower's inability to save a down payment, and poor credit ratings are considerable, especially in small communities where many people may not be participating in the wage-based economy, particularly those Aboriginal people who are engaged in the land-based economy. This becomes a significant barrier for potential borrowers to access mortgage finance.

CONCLUSION

To a large extent, the housing finance issues identified in this study are a reflection of broader challenges posed by the economic, social and geographic characteristics that are specific to the territories. Circumstances such as the small and somewhat transient population, remote and inaccessible locations, harsh climate, weak housing market, uncertain economy, high unemployment and low income in some areas, all contribute to complications in the conventional housing construction and housing financing processes that are commonplace in other regions of Canada. These complications create additional risk to lenders and can be an obstacle to the provision of financing for housing.

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Housing Research at CMHC

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